

Franchise Tax Board**ANALYSIS OF ORIGINAL BILL**

Author: Ducheny Analyst: Angela Raygoza Bill Number: SB 96
Related Bills: See Legislative History Telephone: 845-7814 Introduced Date: January 26, 2009
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: PIT Rates/Modify To 9%, 9.5%, 10%, 10.5%, 11% & 8.5% AMT Rate
Beginning On Or After January 1, 2009

SUMMARY

This bill would modify and add personal income tax (PIT) rates of 9%, 9.5%, 10%, 10.5%, and 11% and would increase the alternative minimum tax (AMT) rate for PIT taxpayers to 8.5%.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to enact higher tax to generate revenue that would address the current budget shortfall.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective upon enactment and operative for taxable years beginning on or after January 1, 2009.

POSITION

Pending.

ANALYSIS**FEDERAL/STATE LAW**

Federal law imposes six different income tax rates on individuals, estates, and trusts ranging from 10% to 35%. Existing state law imposes six different PIT rates ranging from 1% to 9.3%. Each tax rate applies to a different level of income known as a "tax bracket." Existing state law requires the Franchise Tax Board (FTB) to recalculate the tax brackets each year based on the change in the California Consumer Price Index (CCPI).

For taxable years beginning on or after January 1, 1991, and before January 1, 1996, state law included PIT rates of 10% and 11% for taxable income in excess of \$100,000 and \$200,000, respectively. Higher thresholds were applicable for a taxpayer using the head of household filing status. These tax bracket amounts were also indexed for inflation.

Board Position:

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Department Director**Date**

Lynette Iwafuchi

03/13/09

For Selvi Stanislaus

For taxable years beginning on or after January 1, 2005, state law imposes an additional 1% Mental Health Tax (MHT), not subject to reduction by credits, on the portion of a PIT taxpayer's taxable income that exceeds \$1 million. The taxable income threshold of \$1 million is not indexed based on changes in the CCPI. The MHT is subject to estimated tax payment requirements, interest, penalty, and other tax administration rules.

Federal law provides an AMT rate of 26% on alternative minimum taxable income up to \$175,000 and 28% on AMT taxable income exceeding that amount for PIT taxpayers. Existing state law provides an AMT rate of 7% under the PIT law. A taxpayer with substantial income can use preferential tax benefits, such as exclusions, deductions, and credits, to reduce their income tax liability. AMT was established to ensure that a taxpayer who can use preferential tax benefits does not completely escape taxation.

THIS BILL

This bill would establish a PIT rate of 9% for the following:

- Single filers (including married/Registered Domestic Partners (RDPs) filing separate, trusts, and estates) whose taxable income is over \$47,055 and equal to or less than \$60,000,
- Joint filers whose taxable income is over \$94,110 and equal to or less than \$120,000, and
- Head of household filers whose taxable income is over \$64,050 and equal to or less than \$81,670.

This bill would establish a PIT rate of 9.5% for the following:

- Single filers (including married/RDPs filing separate, trusts, and estates) whose taxable income is over \$60,000 and equal to or less than \$125,000,
- Joint filers whose taxable income is over \$120,00 and equal to or less than \$250,000, and
- Head of household filers whose taxable income is over \$81,670 and equal to or less than \$170,145.

This bill would establish a PIT rate of 10% for the following:

- Single filers (including married/RDPs filing separate, trusts, and estates) whose taxable income is over \$125,000 and equal to or less than \$250,000,
- Joint filers whose taxable income is over \$250,000 and equal to or less than \$500,000, and
- Head of household filers whose taxable income is over \$170,145 and equal to or less than \$340,290.

This bill would establish a PIT rate of 10.5% for the following:

- Single filers (including married/(RDPs filing separate, trusts, and estates) whose taxable income is over \$250,000 and equal to or less than \$500,000,
- Joint filers whose taxable income is over \$500,000, and \$1,000,000, and
- Head of household filers whose taxable income is over \$340,290 and equal to or less than \$680,580.

This bill would reestablish a PIT rate of 11% for the following:

- Single filers (including married/RDPs filing separate, trusts, and estates) whose taxable income is over \$500,000,
- Joint filers whose taxable income is over \$1,000,000, and
- Head of household filers whose taxable income is over \$680,580.

Combined with the existing additional 1% MHT, this bill would establish a PIT rate of 12% for taxpayers with income greater than \$1 million.

For example, the tax brackets under this bill (9% through 12% rates) would be as follows:

2009 Tax Brackets And Rates For Single Filers As Proposed			
\$0	-	\$7,168	1.0%
\$7,168	-	\$16,994	2.0%
\$16,994	-	\$26,821	4.0%
\$26,821	-	\$37,233	6.0%
\$37,233	-	\$47,055	8.0%
\$47,055	-	\$60,000	9.0%
\$60,000	-	\$125,000	9.5%
\$125,000	-	\$250,000	10%
\$250,000	-	\$500,000	10.5%
\$500,000	-	\$999,999	11%
\$1,000,000	-	and over	12%

Beginning on or after January 1, 2009, this bill would provide that the 9%, 9.5%, 10%, 10.5%, and 11% brackets would be adjusted annually for inflation.

This bill would also increase the AMT rate from 7% to 8.5% for PIT taxpayers.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would require some changes to existing tax forms and instructions and information systems, which could be accomplished during the normal annual update.

TECHNICAL CONSIDERATIONS

This bill indicates new income bracket amounts and indexing for inflation for taxable years 2009. Indexing for inflation using normal rules would begin in 2010. Amendment 1 has been provided to correct this technical error.

LEGISLATIVE HISTORY

AB 2897 (Hancock, 2008) would have reestablished PIT rates of 10% and 11% and would increase the AMT rate for PIT taxpayers to 8.5%. AB 2897 failed passage out of the Assembly Revenue and Taxation Committee.

AB 6 (Chan, 2005) would have reestablished PIT rates of 10% and 11% and increased the AMT rate for PIT taxpayers to 8.5%, also would have reduced the amount of tax paid under the increased tax rates by the amount of tax imposed under Proposition 63, the MHT. AB 6 failed to pass out of the house of origin by the constitutional deadline.

Proposition 63 (Steinberg), approved by voters in the November, 2004, General Election, imposes a 1% tax on taxable incomes in excess of \$1 million to provide a dedicated funding source for the expansion of mental health treatment options for children, adults, and seniors.

AB 1403 (Coto, 2005), AB 4 (Chan, 2003), and SB 1255 (Burton, 2002) would have reestablished PIT rates of 10% and 11% and would increase the AMT rate for PIT taxpayers to 8.5%. AB 1403 failed to pass out of the Assembly Revenue and Taxation Committee; AB 4 and SB 1255 failed to pass out of the house of origin by the constitutional deadline.

SB 169 (Alquist, Stats. 1991, Ch. 117) increased the tax rates on individuals for taxable years beginning on or after January 1, 1991, and before January 1, 1996, by adding 10% and 11% brackets and increasing the AMT rate from 7% to 8.5%.

PROGRAM BACKGROUND

In the early 1990s, California faced a severe recession, which resulted in significant shortfalls in the state budget. In response, the state acted to increase revenues and reduce expenditures. As one way of increasing revenues, the state imposed a temporary income tax rate increase¹ in 1991, adding 10% and 11% rates for the highest income taxpayers. This temporary tax increase was in effect for four taxable years and sunset for taxable years beginning on or after January 1, 1996.

OTHER STATES' INFORMATION

The states surveyed include *Florida*, *Illinois*, *Massachusetts*, *Michigan*, *Minnesota*, and *New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws.

Florida does not have a personal income tax. *Illinois*, *Massachusetts*, and *Michigan* impose a flat tax of 3%, 5.3%, and 4.35% respectively. *Minnesota* and *New York* have a progressive rate. *Minnesota* has a maximum tax bracket of \$71,591 for single and \$126,581 for joint filers, with a maximum tax rate of 7.85%. *New York* has a maximum tax bracket of \$20,000 for single and \$40,000 for joint filers, with a maximum tax rate of 6.85%.

These amounts and rates apply to returns filed in 2009 for the 2008 taxable year.

¹ SB 169 (Alquist, Stats. 1991, Ch. 117)

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

The revenue gain from this bill would be as follows:

Estimated Revenue Impact of SB 96 Effective On or After January 1, 2009 Enactment Assumed After June 30, 2009 (\$ in Billions)			
Add brackets, increase AMT	2009-10	2010-11	2011-12
	\$2.1	\$2.8	\$4.0

This estimate does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

The revenue impact of this bill would depend on the number of taxpayers that fall into the new brackets.

The above estimates are based on the department's current personal income tax model. The revenue was estimated for future years using projected growth in personal income, and converted to fiscal years for the table above. These estimates incorporate the changes to the alternative minimum tax, as well.

Approximately 9,500,000 returns would be subject to the higher tax rates in the 2009 taxable year, under this bill.

LEGISLATIVE STAFF CONTACT

Legislative Analyst

Angela Raygoza

(916) 845-7814

angela.raygoza@ftb.ca.gov

Revenue Manager

Jay Chamberlain

(916) 845-3375

jay.chamberlain@ftb.ca.gov

Asst. Legislative Director

Patrice Gau-Johnson

(916) 845-5521

patrice.gau-johnson@ftb.ca.gov

Analyst	Angela Raygoza
Telephone #	845-7814
Attorney	Patrick Kusiak

FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO SB 96
As Introduced January 26, 2009

AMENDMENT 1

On page 3, line 15, strike "2009" and insert:

2010